

**DEPARTMENT OF STATE REVENUE****LETTER OF FINDINGS NUMBER: 98-0501  
ADJUSTED GROSS INCOME TAX  
For Years 1992, 1993, AND 1994**

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**ISSUES****I. Adjusted Gross Income Tax – Net operating loss limitations .**

The taxpayer protested the auditor's procedure for importing IRS Section 382 net operating loss carryforward limitations to Indiana adjusted gross income calculations.

**STATEMENT OF FACTS**

Taxpayer corporation is the result of the merger of two corporations doing business in Indiana, with the new corporation continuing to file Indiana returns. As a result of the change in ownership of the two predecessor corporations, taxpayer's Federal net operating loss was limited to a percentage of the purchase price of the predecessor corporations under the Internal Revenue Code Section 382. Taxpayer corporation deducted as its Indiana net operating loss carryover the combined Indiana losses of its two predecessor corporations. The auditor reduced taxpayer corporation's net operating loss by a proportional percentage (said percentage being the percentage of taxpayer's adjusted gross income apportioned to Indiana) of the percentage of the purchase price of the predecessor corporations as allowed by the Internal Revenue Code Section 382. Taxpayer is protesting the auditor's reduction of its allowed net operating loss.

**I. Adjusted Gross Income Tax – Net operating loss limitations.****DISCUSSION**

Two Indiana statutes that specifically refer to IRS sections are at issue. IC § 6-3-1-3.5(b) which defines taxable income for corporations as:

In the case of corporations, the same as "taxable income" (as defined in Section 63 of the Internal Revenue Code) adjusted as follows...

Both the department and taxpayer corporation agree that this federal limitation is applicable to the taxpayer corporation at the federal level and that it applies to Indiana's adjusted gross income. Inasmuch as Internal Revenue Code Section 382- which serves to reduce the Federal net operating loss carryforward following a corporate ownership change or merger – is not explicitly referenced in either of the above statutes, the issue is how it effects the Indiana adjusted gross income tax computations.

Taxpayer corporation takes the position that absent explicit treatment by the above statutes, the Section 382 loss is an allowable unapportioned net operating loss derived from sources within Indiana and taken directly from Indiana adjusted gross income. The auditor took the position that the proportional percentage of the Section 382 amount is the percentage of taxpayer's adjusted gross income apportioned to Indiana in the loss years. Neither calculation is supported by the above statutes.

Consequently, rather than applying a percentage based on a ratio of historical losses, the audit should be calculated based on the apportionment percentage of the year of purchase applied to the federal section 382 limitation (which is long term tax exempt rate to the fair market value of the stock at date of purchase). This methodology parallels federal methodology in that it does not look to historical losses in calculating the loss limitation. Then, as required by IC § 6-3-2-2.6(b), the loss is to be calculated in the same manner that Section 2 of this chapter determines income derived from Indiana, which requires the adjusted gross income for corporations to be apportioned.

### **FINDINGS**

Taxpayer protest denied in part and sustained in part. After the Section 382 limitations are incorporated into the Section 172 net operating loss values, they are then imported into the Indiana adjusted gross income calculation based on the methodology outlined above.